

HELP ?

Swimming against the tide: Crisis management in **Malaysia**

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Abstract:

*Unlike Thailand, Indonesia and Korea, **Malaysia** succumbed to the financial crisis with only a little foreign debt exposure of its banking system. For this reason, it has so far managed to muddle through without an **IMF**-sponsored rescue package.*

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[Headnote]

Unlike Thailand, Indonesia and Korea, Malaysia succumbed to the financial crisis with only a little foreign debt exposure of its banking system. For this reason, it has so far managed to muddle through without an IMF-sponsored rescue package. In the absence of a clear policy anchor, indecisiveness has adversely affected Malaysia's recovery process. The recent dramatic policy shift could usher in long-term recovery only if the breathing space provided by capital controls and pump priming is appropriately used for the speedy implementation of required adjustment policies, in particular recapitalization of troubled domestic banks and revitalizing the debt-laden corporate sector.

Until the onset of the currency crisis, Malaysia was considered the best "development success story" among the second-tier newly industrializing economies (NIEs) in East Asia. While Malaysia's economic performance was impressive by developing-country standards throughout the post-independence period, the achievements were truly remarkable from the late 1980s when there was a decisive shift towards greater outward-- orientation of economic policy. During 1987-96, the Malaysian economy grew at an average annual rate of 8.8%, lifting per capita income from US\$1,850 to US\$4,425. The economy was at virtual full employment for the last six years, with modest inflation (4.5%). Rapid economic growth was accompanied by rising living standards, and improvement in the distribution of income, ameliorating the twin problems of poverty and racial imbalances. In terms of political stability and policy continuity, the stage was well set for advance through an outward-oriented development strategy. Infrastructure bottlenecks, while important, did not seem impenetrable. Malaysia's aim of entering the league of developed industrial nations by 2020 (as envisaged in Prime Minister Dr Mahathir's Vision 2020 Speech) was generally considered feasible (Athukorala forthcoming).

This impressive growth trajectory changed dramatically with the onset of the currency crisis. The currency and stock market turmoil that began in July 1997 was quickly translated into economic collapse. Unlike the other three crisis countries, Malaysia succumbed to the crisis with only a little foreign debt exposure of its banking system (discussed below). For this reason, it has so far managed to muddle through without an IMF-- sponsored rescue package. But in the absence of a clear policy anchor, indecisiveness has adversely affected Malaysia's recovery process. By mid1998, the economy was in recession and there were no signs of achieving currency and share price stability. The stage was set for a dramatic policy turnaround in favour of an unorthodox (and risky) policy posture whose key elements were capital controls and expansionary macroeconomic policy. Ironically, as of mid-1998 prospects for economic recovery in Malaysia in the immediate future were less promising than in Korea and Thailand, which were forced to follow the conventional (IMF) reform.

What happened to Malaysia? Did it simply succumb to a wild speculative attack in the wake of the Thai crisis or were there some fundamental weaknesses in the pre-crisis Malaysian economy that made it vulnerable to the Thai contagion? Has the recovery process been hampered by inappropriate policy responses? What triggered particular policy responses? What are the likely implications of the dramatic policy shift in September? This paper sets out to answer these and related issues.

The paper is broadly organized into three parts. The following section briefly surveys the onset of the crisis and subsequent economic collapse. The next section examines the sources of vulnerability to the crisis and policy responses, with emphasis on their political and institutional underpinnings. The final section discusses the recent policy U-- turn and its likely implications.

From Financial Crisis to Economic Collapse For over five years prior to the onset of the recent currency crisis, the exchange rate of the ringgit varied in the narrow range of 2.36 to 2.51 ringgit (Malaysian dollar, M\$) per US dollar. When the Thai baht came under heavy speculative attack in mid-May, the ringgit also experienced heavy selling pressure. The central bank, Bank Negara Malaysia (BNM), responded with massive foreign exchange market intervention; it sold close to US\$1.5 billion to prop up the ringgit. It held the ringgit firmly through continued market intervention for another week and then gave way to market forces on 14 July by floating. With the ability to defend the currency dramatically reduced, and without any indication as to the depth of the impending crisis, "unleashing the cavalry" was indeed the only sensible policy.

Between the first week of July 1997 and 7 January 1998 when the slide hit bottom (M\$4.88 = US\$1), the ringgit depreciated against the dollar by almost 50%. After showing some signs of stability during February and March, the exchange rate continued to deteriorate with wide swings in the following months (until it was fixed at the rate of M\$3.80 = US\$1). This contrasted with the experience of Thailand and Korea where from March onwards their currencies showed signs of stabilizing at higher levels. The stock market collapse was even more drastic (Fischer 1998; BIS 1998). Between July 1997 and mid-January 1998, the all ordinaries index of the Kuala Lumpur Stock Exchange (KLSE) fell by over 65%, whipping off almost US\$225 billion of share values, the biggest stock market plunge among the five "crisis" countries. There was no improvement in stock prices until the newly-- introduced capital controls brought about some "recovery" in early October 1998.

As a result of the property market crash and massive capital outflows, non-performing loans in the banking system began to increase. According to BNM data, the proportion of non-performing assets increased from about 2% in July to 3.6% in December 1997 and then to 11.8% in July 1998. Market analysts believe, however, that the problem is much more severe than the official figures suggest, as many companies have begun to roll over debt as part of their survival strategy. Independent estimates of the non-performing loan ratio ranged from 25% to 30% by mid-1998 (Heibert 1998; Financial Times, 22 August 1998).

Domestic market oriented industries, and the construction and services sectors were affected by the contraction in domestic demand resulting from the negative wealth effect of weaker stock prices and property market slump, and the net contractionary impact of the significant currency depreciation. The increase in non-performing loans of the financial sectors was reflected in a sharp downturn in borrowing and financing, contributing to the liquidity squeeze. Both traditional export industries (that account for 10% of GDP) and export oriented manufacturing (30% of GDP) have expanded significantly, reflecting the substantial gain in competitiveness through real exchange rate appreciation. But this was not adequate to compensate for the growth retarding effect of domestic deflation.

In October 1997 the government forecast a growth rate of 7% for 1998, but subsequently adjusted this downward to 4-5% in December and again to 2-3% in March this year. The national accounts for the first and second quarters of 1998 recorded 2.6% and 6.8% contraction in the economy compared to the corresponding quarters in the previous years. Based on these figures, the economy is likely to contract by 5% in 1998 the first recession for 13 years.

What Went Wrong?

When the shock waves from Thailand hit Malaysia, the Malaysian economy at first appeared robust, with high growth, low inflation, virtual full employment, and low foreign debt. The country's foreign currency sovereign credit rating was A+, in the same league as Hong Kong.¹ The Malaysian banking system looked much sturdier than those in most countries of the region. The popular view at the time was that the ringgit crisis was a mere reflection of the Thai contagion. However, there is evidence that the contagion was only the "trigger" factor. The Malaysian economy succumbed to the crisis because over time it had become vulnerable to a speculative attack. Once the crisis set in, it was exacerbated by the Malaysian Government's failure to attack sources of vulnerability decisively and restore investor confidence.

Vulnerability By the first quarter of 1997 the real exchange rate in Malaysia had appreciated by about 15% compared to that prevailing in 1987, the first year of the recent high growth phase of the Malaysian economy (Athukorala 1998a). This real appreciation is believed to have been a major factor in setting the scene for the crisis. Such an appreciation implies that the country's economic fundamentals may not permit the authorities to defend the currency successfully in the event of a speculative attack.

There was no massive build-up of overseas debt in Malaysia. In contrast to Thailand and Indonesia, foreign capital inflows to Malaysia over the past ten years have been dominated by foreign direct investment (FDI), rather than shortterm private sector borrowings and portfolio investment. However, in 1996 there was a significant increase in the net inflow of private short-term capital. The capital inflow, driven primarily by the boom in the Malaysian share market, accounted for 43.3% of the total annual capital inflow by the end of 1996 compared to 13.2% in the previous year. Increased reliance on short-term capital naturally increased the vulnerability of the ringgit to speculative attacks because such investments can turn around very quickly and leave the country, thus exerting devaluation pressures.

A key determinant of a country's ability to fight a speculative run on its currency is the volume of its foreign exchange reserves. But in a financial crisis, not only do gross capital inflows dry up, but domestic holders of liquid assets try to convert them into foreign exchange and flee the country. In analysing a country's vulnerability to panic, the strength of a country's reserve position has, therefore, to be assessed in comparison to a broader measure of liquidity. Of various measures, M2 (currency plus demand and savings deposits in commercial banks) is regarded as a "compromise" measure of the liquidity of assets for this purpose (Calvo 1995; Sachs et al. 1996). An increase in the M2/reserve ratio points to a decrease in the country's ability to defend the currency; in other words, an increase in the currency's vulnerability to a speculative attack. By June 1997, the ratio stood at 4.7, compared to around 3.0 at the beginning of the decade. The increase in this ratio has been much faster in more recent years prior to the crisis.²

In terms of the conventional performance indicators, the Malaysian banking system looked robust before the crisis. Non-performing loans (those three months or more in arrears) in the banking system fell from 5.5% in 1995 to 3.9% in 1996, far below the critical level of 15-16% used by the Bank of

International Settlement (BIS) to identify troubled banking systems. By mid-1997, the average capital adequacy ratio for commercial banks, merchant banks, and finance companies were 11.8%, 13.3% and 10.6% respectively, compared to the BIS international standard for the overall financial system of 8%. Foreign currency exposure of the banking system remained low thanks to the BNM policy of specifying stringent net open positions on foreign borrowing. By mid-1997, the aggregate net open position of the banking system was less than 5% of total bank liabilities.

Despite this apparent soundness, the Malaysian banking system had developed two signs of weakness over the three or four years prior to the onset of the crisis: a massive accumulation of outstanding domestic credit and heavy exposure of the banking system to the property sector (real estate, construction and share trading). The annual rate of growth of bank credit to the private sector rose continuously from 18% in 1990 to 33.5% in 1997. The ratio to GDP of outstanding credit increased from an average level of 85% during 1985-89 to 120% in 1994 and then to over 160% when the financial crisis broke out in mid-1997. This was the highest credit build-up among the countries in East Asia. Speculators regard a massive credit build-up of this nature as an indicator of policy makers' reluctance to use the interest rate as a policy tool in the event of a speculative attack on the currency. Rapid build-up of credit in a short period may also imply a growing share of lending to less creditworthy borrowers.³

Rapid credit expansion was accompanied by a sharp increase in the share of total credit going to the property sector (broadly defined to include share market operations and the real estate sector). By the end of 1996, this sector accounted for over 45% of total outstanding bank credit. It is believed that this share could be much higher (around 55%) if unclassified loans to conglomerates, which are normally used to finance property, are appropriately taken into account.

Much of the recent expansion of bank lending to these activities had taken the form of "connected (state-directed) lending" rooted in the long-standing intimate link between the government and business in the country. As part of the strategy of restructuring business ownership under the New Economic Policy (introduced in 1970 and replaced by the National Development Policy in 1990) the Malaysian Government has throughout influenced lending activities of banks (Gomez and Jomo 1997). Such influence gained added impetus to Mahathir's "big push" towards the Year 2020. Off-budget financial support, mostly in the form of government sponsored bank loans, has been a key element of the incentive package offered to industrialists, property developers and Malaysian companies investing overseas as part of this ambitious growth strategy (Holloway 1997).

There has been a rapid expansion in the share market in Malaysia since the late 1980s. By the mid-1990s, with a market capitalization of around US\$200 billion, the Kuala Lumpur Stock Exchange (KLSE) was the third largest in the Asia-Pacific Region after Tokyo and Hong Kong. There were days when the turnover on the KLSE was higher than that in New York. In relation to GDP, stock market capitalization in Malaysia (over 300% of GDP) was substantially higher than any other significant economy (Henderson 1998, p. 21). At the onset of the crisis, foreign investors accounted for only 30-40% of the activities in the market.

Rapid expansion of the share market was not, however, due to initiatives to redress underlying weaknesses of corporate governance. Most of the listed companies in Malaysia are tightly controlled by a handful of powerful families. These families often retain majority stakes even in public companies. Moreover, in many cases the interests of company bosses and politicians are closely interwoven. Manipulation of intercompany share transactions in order to augment profit in privately owned companies at the expense of listed companies has been a common occurrence in the Malaysian

corporate world. Such malpractice makes share trading vulnerable to financial panic because unconnected (minority) shareholders have every reason to worry about how they would be treated in the event of a market downturn. When foreign participants started pulling out to avoid currency risk, the local players got panicky. Based on past experience, the minority shareholders were naturally concerned that in troubled times they might be hardest hit. A number of murky share market dealings in the immediate aftermath of the onset of the crisis compounded this suspicion and thus aggravated the share index slide (The Economist, 20 December 1997, p. 111).

Policy Slippage

The initial response of the Malaysian Government to the outbreak of the currency crisis was one of denial. Given the perceived soundness of economic fundamentals, Prime Minister Dr Mahathir's immediate reaction was to pounce on the villains: currency speculators. By implicating the American financier George Soros (a Jew of Hungarian origin) in the speculative attack, he complained about a Jewish conspiracy to jeopardize the Malaysian miracle. At the IMF and World Bank annual meetings in Hong Kong in late September, Dr Mahathir stated that currency trading (beyond what is required to finance trade) was "unnecessary, unproductive and immoral", and that "it should be made illegal".⁴ Mahathir continued his attack on speculators in domestic and international forums, including the Annual Asia-Pacific Economic Cooperation (APEC) summit on 18 November at Vancouver and the Commonwealth Heads of Government Meeting at Birmingham in the same month. Almost every attack by Mahathir against his perceived enemies precipitated a further sliding of the ringgit.

Even more damaging to investor confidence than the Prime Minister's attacks on speculators were several initiatives to directly intervene in share market operation with a view to punishing speculators. On 27 August, the KLSE banned the short selling of 100 blue-chip stocks and rules were introduced to discourage the sale of stocks: sellers were required to deliver physical share certificates to their brokers before selling and the settlement period was reduced from five to two days. On 3 September, the Prime Minister unveiled a plan to use funds from the Employees Provident Fund (EPF) to prop up share prices by buying stocks from Malaysian shareholders - but not foreigners - at a premium above prevailing prices. These moves backfired, triggering a massive sell-off of stocks in the KLSE and undermining sentiment on other regional bourses. Ironically, government-sponsored share purchases were seen by market participants, both local and foreign, as an opportunity to get rid of Malaysian shares, rather than as a reason for holding onto them.

There was some retreat from this "unorthodox" policy posture during the ensuing months as the crisis deepened. The ban on short selling was lifted in early September. In the same month, the government announced the postponement of some grandiose infrastructure projects amounting to about US\$10 billion. The Budget for 1998 unveiled on 17 October contained some measures to reduce the current account deficit through selective import duties and a "buy Malaysia" campaign. However, the government failed to come up with a coherent programme of reforms to deal with the crisis.

On 5 December, the Deputy Prime Minister and Finance Minister, Anwar Ibrahim, unveiled a reform package. The key elements of the package included cutting government spending by 18%, postponing indefinitely all public sector investment projects which were still in the pipeline, stopping new overseas investment by Malaysian firms, freezing new share issues and company restructuring, and cutting salaries of government ministers by 10%. With these measures, the previous budget forecast of economic growth (7%) was lowered to 4%-5%.

This policy statement undoubtedly marked the most important economic policy shift in the decade.

Despite some misleading inferences in the mass media, this programme was not, however, comparable to the comprehensive IMF-supported policy packages in Thailand and Korea. There was no commitment to raising domestic interest rates to support the currency and to tame inflation. Nor was any concrete strategy proposed for restructuring the financial system.

Resort to a contractionary monetary policy to supplement the significant fiscal austerity measures was ruled out by the heavy reliance of the economy on bank credit. An increase in interest rates was bound to have a severe effect on the debt-ridden private sector firms - and the viability of their banks - which were already suffering from the burst of the real estate bubble and the share market crash. Moreover, given the intimate link between business and government forged under the NEP, the positive stabilizing impact on the ringgit of the increase in the interest rate had to be weighed against its negative effect on politically connected business groups.

In March 1998, an Asset Management Corporation was set up to undertake restructuring and recapitalization of the banking system. But difficulties in obtaining the required funds precluded concrete policy initiatives. BNM continued to cushion the banking sector and debt-ridden companies (against the liquidity squeeze caused by the share market crash and capital outflow) by keeping a lid on interest rates and injecting liquidity into the system by printing money.

Since the onset of the crisis there was an apparent conflict between Dr Mahathir and his deputy and Finance Minister (and heir apparent), Anwar Ibrahim, over how to manage the crisis. Following Mahathir's attack on speculators at the IMF-World bank meeting in Hong Kong, Anwar quickly acted to assure the international investment community that the government would not introduce capital controls. This suggested a policy disagreement at the top for the first time. Subsequently, measures to tame speculators were announced in September by Dr Mahathir alone; Anwar never expressed a view on them. The December 1997 austerity package was announced by Anwar, in a significant departure from the conventional practice of having all important policy announcements made by the Prime Minister. In all these instances the international news media speculated on a possible rift between the two. Many observers are of the view that this apparent conflict contributed to policy indecisiveness in tackling the crisis, and reduced the effectiveness of whatever policy measures were taken by increasing the "political risk premium".

Imposition of Capital Controls and Aftermath

By mid-1998, the degree of freedom available to the Malaysian Government had become severely limited. A planned attempt to issue sovereign bonds in the United States and Europe to raise US\$2 billion for the banking-sector restructuring programme had to be shelved in late August because of the unanticipated downgrading of Malaysia's credit rating by international rating agencies. This was followed by the publication of the second quarter national accounts which brought home the message that the crisis had hit far harder than the government had predicted.

Dr Mahathir now abandoned policy tinkering along conventional lines and embarked on his preferred strategy of capital controls and credit expansion. To set the stage for the policy turnaround, Anwar was sidelined from the policy scene by the appointment of Daim Zainuddin, Mahathir's long-time policy adviser, as the special minister in charge of economic recovery.⁵

In order to stimulate the economy through fiscal and monetary expansion, it was necessary to insulate the domestic interest rate from shortterm capital mobility. As a first step, on 31 August Malaysia effectively barred offshore trading of Malaysian company shares in a move aimed at the over-the-

counter market (OTC) in Singapore, where short selling of Malaysian shares continued despite prohibition of such activities in Malaysia.⁶ (Shares of about 15% of listed Malaysian companies trade on the OTC market, Financial Times, 10 September 1998) This was followed by the imposition of stringent controls over short-term capital transactions (1 September) and fixing the exchange rate at M\$3.80 per U.S. dollar (effective 2 September).⁷ The new capital controls banned trading in ringgit instruments among offshore banks and stopped Malaysian financial institutions offering domestic credit facilities to non-resident banks and stockbrokers. With a view to stopping speculative trading in ringgit in overseas markets (predominantly in Singapore),⁸ it was announced that all ringgit deposits held outside the country would cease to be legal tender after 30 September, and the use of ringgit as an invoicing currency in foreign trade was banned with immediate effect. The amount of foreign exchange approved for travel purposes was limited to the foreign currency equivalent of M\$1,000. The amount allowed for overseas investment without prior approval was limited to M\$10,000 in foreign currency.

The new controls are confined to short-term capital flows. With the exception of limits on foreign exchange for foreign travel by Malaysian citizens, there has not been a retreat from Malaysia's long-standing commitment to an open trade and investment policy. No new direct controls have been imposed on import and export trade. Foreign investors in Malaysia are free to repatriate dividends and equity related to their direct investment in the country.

A week before the introduction of capital controls, BNM reduced the intervention rate on which interest rates are based from 10% to 9.5% and cut the statutory reserve ratio to 6% from 5% in order to inject liquidity into the debt-ridden banking system. In early September it loosened the curbs on lending to property which had been introduced before the crisis began and announced its intention to relax curbs for credit to share market investment. On 9 September BNM advised banks to stimulate the economy by expanding their loans at a rate of 8% a year, beginning this year. Any bank that fails to meet this minimum growth rate is required to provide justification to the satisfaction of BNM. The Malaysian authorities expect the new policy to generate about 1% growth next year.

While Mahathir's expression of interest in capital controls dates back to early in the crisis, the new policy has received a measure of legitimacy from recent developments in the international economic policy debate on crisis management. In an article published in Fortune magazine in July 1998, Krugman argued that capital controls could give the crisis-affected Asian economies a breathing space in which to resume growth. Bhagwati (1998) rekindled the old debate on the appropriate sequencing of economic liberalization in developing countries, arguing that premature capital market liberalization can harm, rather than promote, the successful integration of developing countries into the world trading system. There was also growing attention in the financial press to the fact that China and Taiwan, the two economies in the East Asian growth league with controls on short-term capital movements, fared much better than the rest of the region during the crisis.⁹

However, despite its underlying logic, the new strategy is risky, for a number of reasons. First, as already noted, the rationale behind the imposition of capital control is to avert a painful economic collapse and to provide a conducive setting for the implementation of the required adjustment policies, in particular banking sector restructuring. The danger is that the complaisance induced by temporary recovery through expansionary policies may lead to postponement of long-term structural reforms, and thus to long-term economic deterioration. Second, any form of market intervention of this nature involves economic costs associated with bureaucratic controls and related rent-seeking activities. And prolonged use of controls invariably compounds the economic costs (Hill 1998). Third, the scope for avoidance and evasion is vast. In the context of an economy like Malaysia that remains highly integrated in the world economy through trade in goods and services, through foreign direct investment, and

through flows of remittances from migrant workers, controls on capital flows are difficult to enforce.

Fourth, perhaps the most risky element of the new reform measures is its fixed exchange rate commitment. The motive behind fixing the exchange rate is to provide a nominal anchor for the price system. However, there is unlikely to be a significant strengthening of the exchange nominal rate through the "announcement effect" of the new fixed rate, because it has been implemented as part of a policy package whose prime aim is to inflate the economy through "pump priming". More importantly, under this strategy, domestic inflation could be reflected in a real exchange rate appreciation. In that case, the cost of adjustment will fall disproportionately on the tradable sector, hindering an export-led recovery. Expectations of future adjustment of the nominal rate, to counter this effect, are liable to induce capital flight and reserve depletion, making the entire policy package unsustainable (Dornbusch and Edwards 1994).

Many commentators have expressed the fear that the new policy may hamper economic recovery by adversely affecting foreign direct investment in Malaysia. Any policy measure that constitutes a significant departure from a longstanding commitment to economic openness could certainly impact adversely on the general investment climate of the country. However, whether this would be translated into a significant reduction of FDI flows remains debatable. The pessimistic view is based on a false aggregation of FDI with portfolio investment and short-term bank credits. FDI flows are determined by longterm considerations governing international production decisions of MNEs, not by financial panics and related short-term economic changes. What is primarily important for attracting FDI is a firm commitment to the maintenance of an open current account.

However, the political and policy uncertainty created by the ousting of Anwar and the subsequent legal actions against him may prove to be much more damaging to the confidence of long-term investors in the Malaysian economy. Until recently, Malaysia had "the vast advantage" over other Southeast Asian countries of a federal structure, democratic legitimacy and the rule of law (Radelet and Sachs 1997, p. 56). Politically, Dr Mahathir still holds all the cards and he should be able to assure himself of a convincing victory in the forthcoming general elections, but serious doubts raised by recent events about the democratic and legal process of the country will continue to pervade the policy scene for some time.

[Footnote]

NOTES

[Footnote]

Thanks are due to Harold Crouch and Peter Warr for very helpful comments on an earlier draft. 1. Standard and Poor's foreign currency sovereign credit ratings for the other crisis countries as at end May 1997 were: South Korea AA-, Thailand A, Indonesia BBB and Philippine BB+ (Far Eastern Economic Review, 29 May 1997, p. 60). 2. The conventional yardstick for the adequacy of reserves used in the literature on balance of payments issues is the import-month equivalent of reserves (the ratio of reserves to one month's worth of imports). This measure is not appropriate for the present analysis because a run against currency is rarely associated with an import spree (Calvo 1995).

[Footnote]

3. Note that financier George Soros pointed to massive private sector credit accumulation as the main weakness of the Malaysian economy. See the reference given in footnote 4. 4. George Soros responded to Mahathir, saying that "interfering with the convertibility of capital at a moment like this is a recipe for disaster" and that Dr Mahathir was "a menace to his own country". For excerpts from statements made by Mahathir and Soros at the IMF meetings, see FPB (1997). 5. On 3 September Anwar was removed from the positions of Deputy Prime Minister and Finance Minister. He was subsequently expelled from the ruling UMNO party by invoking Article 18 of the party constitution. (Article 18.4(f) states that UMNO members must always safeguard the good name of the party and Article 18.4(g) states that members must at all times reflect good ethics.) On 8 September, Mahathir appointed himself the first Finance Minister, but the position of deputy Prime Minister still remains vacant. 6. This move prompted the resignation of the governor and the deputy governor of BNM. 7. The new fixed rate represented an appreciation of 10.5% against the market rate at the time. But the rate of depreciation against the pre-crisis rate was almost 39%. 8. At the time of introducing these controls, ringgit deposits in Singapore were estimated at around M\$25 billion (or US\$6.6 billion at the new exchange rate).

[Footnote]

9. In a special briefing to the press following the introduction of capital controls, Special Function Minister Ibn Daim Zainuddin

stated that the controls were introduced to avoid political instability which could lead to economic collapse (Star, 5 September 1998). He stated that before introducing currency controls, they had studied the systems in Chile, Slovenia and China, and decided that the Chinese model would be the best option for Malaysia.

[Reference]

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